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In the

Supreme Court of the United States

OCTOBER TERM, 1948

No. 335

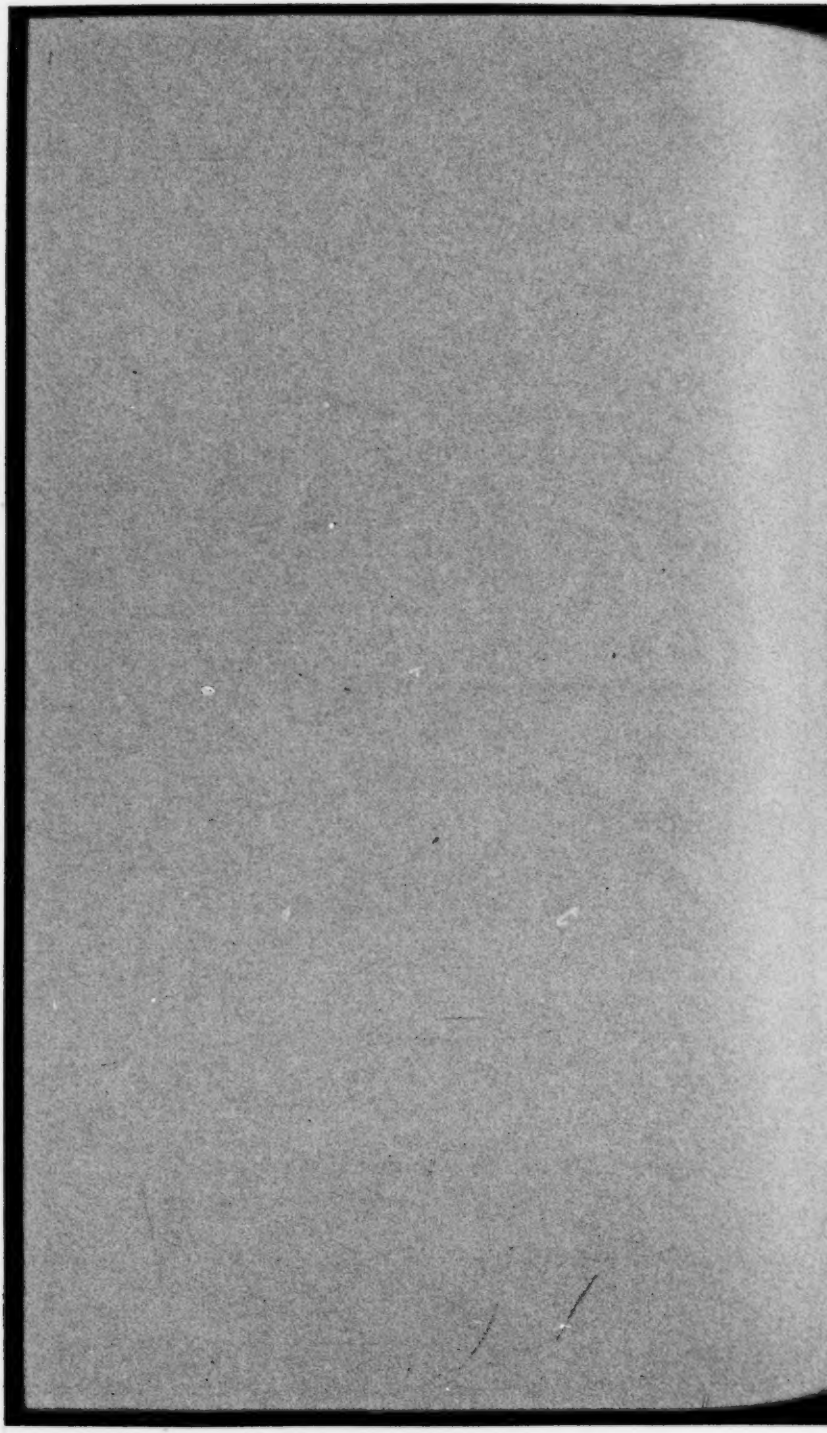
EDGAR B. WHITCOMB, ANNA S. WHITCOMB and HENRY J. HELMERS, JR.,
Petitioners,
vs.
EARL L. CLARK, Drain Commissioner of Oakland County, STATE LAND OFFICE BOARD, INTERURBAN LAND COMPANY, LAWRENCE WESTPHAL, EUGENE W. KNAPP and BEULAH V. KNAPP, his wife, CITIES OF ROYAL OAK, PONTIAC, FERNDALE, BIRMINGHAM, BLOOMFIELD HILLS, BERKLEY, OAK PARK, HAZEL PARK, CLAWSON, PLEASANT RIDGE and HUNTINGTON WOODS, TOWNSHIPS OF SOUTHFIELD, BLOOMFIELD, TROY and ROYAL OAK, COUNTY OF OAKLAND, CHARLES M. ZIEGLER, State Highway Commissioner, ASHTON J. BERST and EDWIN H. WATERHOUSE,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF MICHIGAN AND BRIEF IN SUPPORT THEREOF

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PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF MICHIGAN

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Your petitioners, Edgar B. Whitcomb, Anna S. Whitcomb and Henry J. Helmers, Jr., pray that a writ of certiorari issue to review the judgment of the Supreme Court of Michigan in a cause entitled Earl L. Clark, Drain Commissioner of Oakland County, Plaintiff and Appellee, v. Cities of Royal Oak, Pontiac, Ferndale, Birmingham,

Bloomfield Hills, Berkley, Oak Park, Hazel Park, Clawson, Townships of Southfield, Bloomfield, Troy and Royal Oak, County of Oakland, Charles M. Ziegler, State Highway Commissioner, State Land Office Board, Interurban Land Company, Lawrence Westphal, Eugene W. Knapp and Beulah V. Knapp, his wife, Defendants and Appellees, Edgar B. Whitcomb, Anna S. Whitcomb and Henry J. Helmers, Jr., Defendants and Appellants, Cities of Pleasant Ridge and Huntington Woods, Ashton J. Berst and Edwin H. Waterhouse, Defendants and Cross-Appellants, No. 44,318, which was entered June 29, 1949, decision of which is reported 325 Mich. 298 (p. 303 of Transcript of Record filed herewith.) Petitioners ask that such judgment be reviewed on the ground that the Supreme Court of the State of Michigan refused to give full faith and credit to a judgment of the District Court of the United States for the Eastern District of Michigan, Southern Division, in Bankruptcy.

ACTION IN THE STATE COURTS

Summary Statement

Earl L. Clark, as Drain Commissioner of Oakland County, filed a petition in the Circuit Court for Oakland County, Michigan, in Chancery, seeking a declaratory decree concerning his duties in carrying out the terms of an agreement made with holders of refunding bonds and certificates of indebtedness issued by Royal Oak Drain District. The numerous parties named in the title of the cause, as above set forth, were either holders of such securities or parties subject to taxes for the payment of said obligations. Petitioners were sued as representatives of the entire class of holders of such securities.

Pleadings and proofs developed the following state of facts: In 1939 the said drain district was insolvent, within the meaning of Chapter IX of the National Bankruptcy Act. (U. S. C. A. Sections 401-4, Title 11.) To a considerable extent such insolvency was due to refusal or inability of owners of approximately two-thirds of the land in the district to pay installments of assessments previously made for said drain. It was then apparent that the owners of such lands would permit them to go to tax sales pursuant to foreclosure decrees, as provided in Act 114 of Public Acts of Michigan, 1937, as amended; that at such sales the State of Michigan would become the absolute owner of said lands, free of all prior encumbrances and liens, and that such lands would be sold by the State Land Office Board, a state agency, under Act 155, Public Acts of Michigan, 1937, as amended, and that the proceeds of such sales distributable to the drain district, together with its other resources, would not be sufficient to pay the debts of the district.

As alleged and proven in the state courts, Mr. Clark, who was then, as now, Drain Commissioner, took proceedings in the year 1939 in behalf of said district to obtain a debt adjustment pursuant to Chapter IX of the Bankruptcy Act. Authority to take such action was given by the state, in Act 72, Michigan Public Acts of 1939. By proceedings regularly taken, a plan of composition was confirmed by the appropriate federal court in bankruptcy, and approved by the Michigan Public Debt Commission, a state agency charged with the duty of supervising the creation and modification of funded debts of local taxing agencies within the state. (Act 13, Michigan Public Acts, 1932, First Extra Session.)

The decree of confirmation, which the bankruptcy court entered contained the finding required by Sec. 403(e),

Title 11, Ch. 9, U. S. C. A. that the petitioning district was authorized by law to take all action necessary to be taken by it to carry out the plan of composition, so confirmed.

This plan of composition provided for the refunding of the entire debt of the district, over and above a certain amount of cash, distributable against past due interest, and in order to augment resources to a sum sufficient to pay the obligations evidenced by the refunding securities, required annual additional levies to commence in 1947. The paragraph so providing was number 8 of the amended plan of composition, (Tr. 38), which was carried over in identical language and became paragraph 7 of the basic order of the Drain Commissioner made subsequent to the decree of confirmation (Tr. 56). It is fully set out in the lower court's opinion (Tr. 306).

This may not be readily understood without some preliminary explanation. It was based upon a statute, Act 129 Michigan Public Acts of 1939, set out in the opinion (Tr. 312), which requires additional levies of drain assessments to service refunding securities which drain districts are permitted to issue. It specifies that they must be levied on the same percentages initially determined in the proceedings, and be sufficient to pay interest and maintain a sinking fund for ultimate retirement. As there remained a certain amount of the original assessments unpaid, but collectible, these were extended into a supplemental roll to fall due in reduced annual amounts but over a longer period. A formula was embodied in paragraph 8 of the confirmed plan, whereby an annual accounting was to be made each year commencing in 1947, which should take into consideration the net amount of the debt unpaid, the amount collectible on the next annual levy under the supplemental roll, the next year's interest

requirements, and the proportionate amount necessary to add to the sinking fund to provide for ultimate retirement. Upon the basis of this calculation an additional levy was to be made, in an amount which, when combined with the levy permitted under the supplemental roll, would prevent interest default and provide for proportionate retirement of principal, which could be accomplished by the call of securities, or purchase of them if they could be obtained below par.

As then anticipated, and as subsequent events have proven correct, the land which would go to the state at tax sales, would be restored to private ownership. No question was then entertained as to these lands being fully taxable for all purposes as soon as such restoration should occur. There were then no court decisions dealing with the subject, and the applicable statutes, Act 129, Michigan Public Acts 1939, Sec. 67a, Act 282, Michigan Public Acts 1939, and Sec. 7, Act 244, Michigan Public Acts 1939, seemed to justify the conclusion that all privately owned lands, irrespective of their source of title, would be subject to the additional assessments provided in paragraph 8 of the Plan of Composition. The plan was proposed and accepted with this understanding, and presumably approval was granted by the state public debt commission, and by the bankruptcy court on the same basis.

The Michigan Supreme Court in decisions rendered subsequent to the refunding, provided in the plan of composition, adopted a theory as to the meaning of Michigan statutes, which was different from the understanding referred to above. In effect these seemed to hold that land acquired by the state at tax sales, when resold at the state's auction sales, called "scavenger sales", were freed of the possibility of additional assessments for the

payment of existing bonded debts notwithstanding charter or statutory requirements for such levies. Furthermore, that other lands and political units would be subject to no greater additional assessment than if there were no exempt lands. Such decisions are cited in the opinion of the lower court (Tr. 311).

The drain commissioner filed his petition for a declaratory decree on the theory that these subsequent decisions so curtailed his power to levy additional assessments that there must necessarily be a large discrepancy between debt and collectible resources, and as this deranged other features of the plan, he sought instructions as to what should be done (Tr. 20). During the course of the proceedings this discrepancy appeared as approximately $600,000 (Tr. 261). Bondholder defendants (petitioners for this writ) contested the assumption of limitation of the taxing power, insisting *inter alia* that the bankruptcy court decree was a binding adjudication that the provision as to additional assessments was fully authorized by the law of the state.

There were numerous issues in the case which involved only the laws of the state of Michigan, unnecessary to refer to here. The decree of the trial court (Tr. 203) sustained the contention of the drain commissioner as to the exempt status of those properties which had previously been state owned, and the limitation of liability as to other properties and municipalities.

This decree was affirmed by the judgment of the Michigan Supreme Court, which petitioners here seek to review. In both courts, petitioners contended that the Bankruptcy Court decree, in its finding referred to above as to legal power to perform the plan of composition, was *res judicata* and binding upon the drain district, its

officers, and members. The Supreme Court of the State of Michigan recognized this contention, but rejected it, saying (Tr. 312):

> "Appellants (meaning petitioners here) further contend that the decree of the Federal Court approving the plan of composition determined that the drain commissioner had the power to levy such additional assessments, and that such decree is binding on the parties to this suit. Even if the taxpayers were bound by the decree of the Federal Court in the composition proceedings, such decree would not be binding as to the rights and duties of the drain commissioner under state laws, the construction and interpretation of which by the state courts are binding on the Federal Courts. In *Bloomfield Drain District v. Keefe*, 119 F. (2) 157, it was held, 'Decree of Michigan Courts construing the Michigan County Drain Law were binding on Federal Court in action on drain district bonds.' (Syllabus.) See also *Erie R. R. Co. v. Tompkins*, 304 U. S. 64, 58 S. Ct. 817."

Had the court accepted petitioners' contention, the decree of the trial court would have been modified to direct the drain commissioner to levy the additional assessments in the manner and to the extent required by that provision of the plan of composition summarized above. No other portion of the court's opinion than that last quoted is put forth as justification for disregarding the binding effect of the decree of the bankruptcy court.

JURISDICTION

This petition for a writ of certiorari is filed within three months of the time when said judgment was rendered. Presented herewith is a certified copy of the entire record and proceedings in the Supreme Court of Michigan, which is the highest court in said state in which a decision in the case could be obtained.

(3) This petition is filed under the provisions of Title 28 U. S. C. ~~A.~~, Section ~~344(b)~~. It invokes that portion thereof which authorizes review by this court where petitioners are denied rights, privileges and immunities specially set up and claimed under an authority exercised under the United States. Decisions of this court sustaining the jurisdiction here claimed are numerous. Among them the following may be cited:

Chandler v. Peketz, 297 U. S. 609, 56 S. Ct. 602;
Stoll v. Gottlieb, 305 U. S. 165, 59 S. Ct. 134;
Meyer v. Int. Trust Co., 263 U. S. 64, 44 S. Ct. 86.

FEDERAL STATUTE INVOLVED

The portion of Section 403(e), Chapter IX, Title 11, U. S. C. A. existing in 1941 believed applicable is:

> "At the conclusion of the hearing, the judge shall make written findings of fact and his conclusions of law thereon, and shall enter an interlocutory decree confirming the plan if satisfied that (1) it is fair, equitable and for the best interests of the creditors, and does not discriminate unfairly in favor of any creditor or class of creditors; (2) complied with the provisions of this chapter; (3) has been accepted and approved as required by the provisions of subdivision (D) of this section; (4) all amounts to be paid by the petitioner for services or expenses inci-

dent to the composition have been fully disclosed and are reasonable; (5) the offer of the plan and its acceptance are in good faith; and (6) the petitioner is authorized by law to take all action necessary to be taken by it to carry out the plan. If not so satisfied, the judge shall enter an order dismissing the proceedings."

QUESTION PRESENTED

Concisely stated, the question presented to this court is as follows:

Where a plan of composition under Sec. 403(e), U. S. C. A., Title 11, Ch. IX, contains provisions for levying taxes to pay refunding securities, and such plan of composition is found by the decree of the court to be fully authorized by law, does such decree constitute a binding adjudication against the district, its members and officers that the taxing power may be exercised to the extent provided in such plan?

ASSIGNMENTS OF ERROR

The Supreme Court of Michigan erred:

1. In holding generally that final judgments of a federal court based upon an erroneous interpretation of state laws are subject to collateral attack, in the state courts.

2. In denying to a federal court jurisdiction to determine the taxing power which may be exercised in behalf of a petitioning debtor incident to a plan of composition under Ch. IX of the National Bankruptcy Act.

3. In excluding from the binding effect of such a decree the officer whose duty it is to levy the taxes necessary

to perform the plan of composition confirmed by such decree.

REASONS FOR ALLOWANCE OF THE WRIT

In view whereof, petitioners respectfully urge that the writ should issue because:

1. In so affirming said decree, the lower court erroneously decided a question arising under a Federal Statute adversely to petitioners' contentions, and it is believed contrary to the purpose and intent of Congress and the decisions of this Court.

2. The matter at issue is of much importance, since the determination thereof enters into and affects a jurisdiction conferred upon federal courts, in bankruptcy, in connection with debt adjustment proceedings instituted by taxing districts under Chapter IX of the Bankruptcy Act. A determination of this issue is essential in order that creditors of a taxing district obliged to accept plans of composition may have the protection guaranteed to them by the Acts of Congress.

3. The decision and opinion of the Supreme Court of Michigan deprives parties to judgments rendered in the federal courts, and particularly those judgments rendered in debt adjustment proceedings under Chapter IX of the Bankruptcy Act, of rights, privileges and immunities under an authority of the United States.

Submitted herewith is a brief in behalf of petitioners, to which reference is prayed, for a discussion of the law involved and authorities in support of the right claimed by petitioners.

Wherefore, petitioners respectfully request that this court issue a Writ of Certiorari to the Supreme Court of the State of Michigan, to send to this court a full and complete transcript of the record herein, (unless the transcript filed herewith shall be deemed sufficient,) to the end that the cause may be reviewed and determined by this court as provided by law, and that the judgment may be reversed with costs, and for such other and further relief as may be appropriate and granted in the premises.

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BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

I.

OPINIONS OF THE COURTS BELOW

Trial Court's Opinion (Tr. 193). Only last four paragraphs are pertinent to the matters in issue here. The Court amplified this at the time the decree was signed (Tr. 268) by stating that the decision of the Michigan Supreme Court in *Keefe v. Drain Commissioner*, 300 Mich. 503, must be followed, but that he considered it an erroneous interpretation of Michigan statutes and constitution.

Opinion of Supreme Court of the State of Michigan (Tr. 303), officially reported 325 Mich. 298. Only portion thereof which presents federal question sought to be reviewed is first paragraph on page 312 of Transcript.

II.

DATE OF JUDGMENT TO BE REVIEWED JUNE 29, 1949 (Tr. 302)

The statutory provision and authorities believed to sustain jurisdiction appear in accompanying petition under heading of "jurisdiction" (*supra* p. 8).

III.

The recital of facts contained in accompanying petition under heading "Action in State Courts. Summary statement" is believed sufficient, so far as it relates to the federal question. The opinion (Tr. 303) gives a more complete statement of all facts and issues presented to the

Supreme Court of Michigan. Essential facts presenting question for review here are the following:

1. Confirmation of plan of composition by federal court decree in bankruptcy proceedings under Ch. IX of the Bankruptcy Act. By the plan of composition the taxing district undertook the levy of taxes sufficient to meet requirements of securities issued pursuant to plan. Decree found the legal authority for such levy in its statement that "petitioner is authorized by law to take all action necessary to be taken by it to carry out the plan of composition, as amended."

2. Plan of composition put into effect.

3. Subsequent decisions of Michigan's highest state court, which indicate limitations on taxing power in behalf of district, which if given effect make it impossible to perform the plan of composition.

4. Rejection by Michigan Supreme Court of the binding effect of the bankruptcy decree, on the ground that it is based on an erroneous conception of Michigan law.

ARGUMENT—SUMMARY

Points relied upon to show error reviewable by this court are set forth in the Assignments of Error appearing in the accompanying petition. Stated as propositions, they are:

1. Federal court judgments are not open to collateral attack because based upon erroneous interpretations of local law.
2. Bankruptcy court has jurisdiction, under Chapter IX of the Bankruptcy Act, to determine the taxing power which may be exercised in behalf of the petitioning taxing district.
3. Bankruptcy decree binds taxing official charged with duty of exercising such taxing power.

In addition to the foregoing, petitioners urge the importance of the question to be settled by the review sought.

I.

FEDERAL COURT JUDGMENTS NOT OPEN TO COLLATERAL ATTACK BECAUSE BASED UPON ERRONEOUS INTERPRETATION OF LOCAL LAW

The Michigan Court refuses to recognize the binding effect of the decree in the bankruptcy proceedings on the broad ground that decrees and judgments in federal courts which declare the duties of state officers under state laws may be disregarded in the state courts, when pleaded as a former adjudication. Citation of *Bloomfield Village Drain District v. Keefe,* 119 F.(2) 157, and *Erie R. R. Co. v. Tompkins,* 304 U. S. 64, 58 S. Ct. 817 suggests confusion and misapplication of the rule declared in those

decisions. Error in determining the applicable state law has never, prior to the opinion in this case, been asserted as a ground for collateral attack upon a judgment of a federal court. If we grant that it is within the jurisdiction of a federal court to determine the state law applicable to the facts presented, as we must in many types of cases submitted to these courts, then it logically follows that an erroneous decision on the question has no different effect than any other error in the case, whether of law or fact. The judgment binds the parties and those in privity with them, until reversed or set aside in a direct proceeding.

It is rather surprising that the Michigan Supreme Court should have fallen into this error, as previously its decisions have fully recognized the binding effect of federal court judgments, even though it considered them erroneous. The most notable recent example of such recognition occurred in a case somewhat similar to this, *Real Estate Exchange Corp. v. Drain Commissioner,* 304 Mich. 596, where it reversed a decree enjoining the levy of a tax to pay a federal court judgment against a drain district. The levy was being made as a result of a mandamus order of the federal court, and although the State Supreme Court was of the opinion that the order was erroneous under state law, it recognized its binding effect as to the district, its officers and taxpayers. The majority opinion in this case states the rule correctly as follows:

> "Although the Federal Court judgment before us may be erroneous, it is not for this reason alone subject to collateral attack."

In support of this the Court quotes from *Fauntleroy v. Lum,* 210 U. S. 230, 237, 28 Sup. Ct. 641, 643.

While no mention of this prior decision is contained in the lower court's opinion in this case, it is obvious that it is inconsistent with the present opinion. We call the Court's attention to it because it contains a comprehensive statement of the rule, which we think ought to govern this case.

Departure from the sound principle expressed in this earlier decision of the Michigan Court seems to us to stem from a failure to distinguish between rules of decision, and *res judicata*. Had petitioners been merely citing the decree as a judicial precedent and urging that it be followed as such, we could have no complaint to this court because it was not followed. What petitioners did was to rely upon the decree as a former adjudication binding upon the parties and those in privity with them, which could not be relitigated.

As indicated in *Meredith v. City of Winterhaven*, 320 U. S. 228, 64 S. Ct. 7, federal courts in the exercise of their jurisdiction cannot escape the duty of deciding questions of state law arising in litigation properly before them. No matter how difficult the question may be, how uncertain the law is, or how fraught with the possibility of subsequent conflict, the duty must be performed.

The decision in this case presents a serious challenge to federal jurisdiction which should not be ignored. Parties to litigation in federal courts ought to be protected in rights adjudicated in their favor, upon any subject within the scope of the courts' jurisdiction, unless such adjudication is reviewed in the manner prescribed by Congress. The effect of this decision is an assumption by the state courts of authority to review such judgments, and vacate them in whole or in part, whenever deemed by them to be based on erroneous conceptions of state law.

II.

BANKRUPTCY COURT HAS JURISDICTION UNDER CH. IX OF BANKRUPTCY ACT TO DETERMINE TAXING POWER WHICH MAY BE EXERCISED IN BEHALF OF PETITIONING TAXING DISTRICT

A complete presentation of petitioner's claims requires a consideration of the jurisdiction of the Federal District Court in these debt adjustment proceedings. It also refutes an argument which we anticipate respondents will urge in support of the lower court's decision.

It was suggested that the bankruptcy court only possessed jurisdiction to determine the validity of consents to the plan of composition, the good faith of the parties, fees and expenses to be allowed, and to supervise the immediate exchange of securities, and cash payments. The provision in Sec. 403(e), U. S. C. A. Title 11, Ch. IX, requiring a finding of legal authority to perform the plan was not, according to this contention, intended to give the court authority to bind anyone to the matter so found, but only to determine whether the proceedings should be dismissed or go forward.

We believe that this contention must be rejected.

On broad grounds of estoppel a litigant who assumes and succeeds in maintaining a certain position in a legal proceeding cannot afterwards assume a contrary position simply because his interests have changed, especially if it is to the prejudice of the party who acquiesced in the position formerly taken. *Davis v. Wakelee,* 156 U. S. 680, 39 L. Ed. 578, 15 S. Ct. 555. The drain district was obliged to seek just such a decree as was entered, if it desired to obtain a modification of its contracts of indebtedness. Postponement of maturity, reduction of interest,

and other benefits to the district prejudices the creditors and thus supplies the ground for estoppel.

No claim may be made of absence of state authority given to its taxing agencies to invoke Ch. IX, or to propose plans of composition, which modify the taxing arrangement, or to be bound by such plans when confirmed. Act 72, Michigan Public Acts 1939, meets all such requirements.

Chapter IX must be construed in the light of its evident purpose abundantly disclosed by its terms and its legislative history. Relief to taxing agencies unable to meet maturing obligations, and suppression of obstructive tactics by minority groups of creditors, was the design of this chapter. At the same time Congress carefully safeguarded the interests of all creditors to prevent abuses on the part of public debtors, intent only on obtaining more favorable terms from their creditors. The court was required to find that the plan confirmed was in their interest as a class. It could not well do so, unless it also found that the promises therein contained were within the district's legal capacity to perform. It is not to be supposed that Congress intended that all creditors should be bound by the confirmed plan, (as it expressly provides) without a correlative obligation on the part of the debtor to respect the plan and abide by it. A declaration of validity was therefore required, which would set at rest all objections by any party to the legality of the covenants contained in the plan.

This declaration of validity in this case was made upon the basis of the identical state statutes, which the Michigan courts have now interpreted as invalidating the plan. The decree of the federal court was made in 1941, and this we believe adjudicates for all time the meaning and

effect of the statutes then in existence, relating to the taxing power which could be exercised in behalf of this drain district.

There is nothing unusual, or contrary to judicial authority for legislative bodies to provide for validation proceedings in advance of issuance of municipal securities, or to authorize declaratory decrees respecting the meaning and application of statute, ordinance, etc. We think that it was plainly the intent of Congress to require the finding as to legal authority, in order to prevent such repudiation as has occurred in this case. In a word to assure creditors that no legal obstacle would prevent the debtor from performing the undertaking which it assumed.

III.

BANKRUPTCY DECREE BINDING UPON TAXING OFFICIALS CHARGED WITH DUTY OF EXERCISING TAXING POWER

There seems to be an assumption by the lower court, and by counsel for respondents, that the decree would not bind the drain commissioner because he was not a formal party to the proceedings. If we are correct in the point asserted, above, that the decree binds the district, then it must follows that it binds its members, and its agents. In fact, the Michigan court seems to recognize its binding effect on members, thus applying the principle declared in its prior decision, *Real Estate Exchange Corp. v. Drain Commissioner (supra)*, wherein it said:

> "Plaintiffs", meaning the taxpayers, "do not urge that the drainage district did not represent them in the federal litigation, nor can such claim be made. * * * It necessarily follows that the district represented the taxpayers in the federal litigation,

and plaintiffs are bound by the federal judgment to the same extent that the district is bound. See also *Holt County v. National Life Insurance Company*, 25 C. C. A. (80 Fed. 686), *Ashton v. City of Rochester*, 133 N. Y. 187 (30 N. E. 965, 31 N. E. 34, 28 Am. St. Rep. 619), *Caldwell v. Guardian Trust Co.* (C. C. A.), 26 F. (2) 218."

It would be incongruous to regard both the district and its members bound by the decree, but not the drain commissioner. He conducted the proceedings in behalf of the district, formulated the plan of composition, and urged its confirmation. However, in addition to this, we believe it must be held that the estoppel of former judgment applies to all agents of the principal which sought and obtained such judgment, insofar as they have duties to perform, to carry out its terms. If that were not true, every corporation would escape from the binding effect of judgments, by having their agents refuse to perform them.

IMPORTANCE OF QUESTION TO BE DECIDED

Petitioners are clearly within Rule 38, 5a, in submitting this petition. A limitation of the binding effect of federal court judgments such as is involved in the portion of the opinion above quoted is not in accord with applicable decisions of this court. The question of the jurisdiction of the bankruptcy court in proceedings under Ch. IX to make binding declarations as to the taxing power which may be exercised in performing a plan of composition has not heretofore been determined by this court. Such question ought to be determined so that creditors may know how far they may rely upon such decrees and if there is any insufficiency in the statute so that Congress may correct it.

We submit that the accompanying petition for certiorari should be granted.

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EARL L. CLARK, Drain Commissioner of Oakland County, STATE LAND OFFICE BOARD, INTERURBAN LAND COMPANY, LAWRENCE WESTPHAL, EUGENE W. KNAPP and BEULAH V. KNAPP, his wife, CITIES OF ROYAL OAK, PONTIAC, FERNDALE, BIRMINGHAM, BLOOMFIELD HILLS, BERKLEY, OAK PARK, HAZEL PARK, CLAWSON, PLEASANT RIDGE and HUNTINGTON WOODS, TOWNSHIPS OF SOUTHFIELD, BLOOMFIELD, TROY and ROYAL OAK, COUNTY OF OAKLAND, CHARLES M. ZIEGLER, State Highway Commissioner, ASHTON J. BERST and EDWIN H. WATERHOUSE,
Respondents

REPLY BRIEF FOR PETITIONERS

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In the

Supreme Court of the United States

OCTOBER TERM, 1949

No. 335

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In order to clarify certain matters which might confuse the court as a result of reading the brief submitted by the Attorney General for the State of Michigan, we submit herewith a reply.

JURISDICTION

(Unless otherwise indicated, numbers in parentheses refer to pages of the transcript)

Respondent suggests (p. 9 of the opposing brief) inadequacy in the method of raising the federal question. Ap-

parently paragraph 26 of Helmers' answer (109) is overlooked. In this he claimed the benefit of the decree in the bankruptcy proceedings. Both trial court and Supreme Court referred to this contention, and overruled it (200, 312).

This court has consistently ruled that the federal question is adequately presented when the opinion of the lower court considers it and decides it contrary to the contention of the petitioner, irrespective of how it was presented.

San Jose L. & W. Co v. San Jose Ranch Co., 189 U. S. 177;
Miedreich v. Lauenstein, 232 U. S. 236;
Whitfield v. Ohio, 297 U. S. 431;
Nickey v. Mississippi, 292 U. S. 393.

The substantial character of the federal question is denied by the opposing brief on the ground that it has already been passed upon in *Municipal Investors Assn. v. City of Birmingham*, 316 U. S. 153, and *Keefe v. Clark, Drain Commissioner*, 322 U. S. 393. The facts in those cases did not involve a decree of confirmation in debt adjustment proceedings, and no indication is contained in them as to what the court's holding would be as to the effect of such a decree.

MERITS OF THE CASE

Respondents' brief attempts to convince the court that petitioners have no meritorious ground to complain of the judgment of the lower court. This is done by suggesting that irrespective of the grounds asserted by the lower court in refusing to treat the decree of the bankruptcy court as

res judicata, this court should find that such a decree binds only the taxing district, but not its officers, agents or constituent members, and is not a final decree.

All this, we submit, is a federal question, calling for an interpretation of Chapter IX of the Bankruptcy Act. Was it the intent of Congress, in providing for the decree of confirmation of a plan of composition, to bind only the creditors, but to leave unaffected those agents who alone can perform the covenants contained in the plan, and the constituent members? Obviously such a decree would be meaningless unless all parties normally in privity with the district were bound by it. Privity on the part of taxpayers seems to be recognized in the lower court's opinion, consistent with its prior decision in *Real Estate Exchange Corp. v. Drain Commissioner,* 304 Mich. 596, referred to on pages 16 and 20 of our petition and brief. Privity of officers is well settled in *Tait v. Western Maryland Railway Co.,* 289 U. S. 620, and *Sunshine Coal Co. v. Adkins,* 310 U. S. 381.

Because the decree was called an interlocutory decree, does not impair its binding effect. Referring to paragraphs e and f, Sec. 403, Ch. IX, Title 11, U. S. C. A., we see that it is an appealable decree and that it binds creditors as soon as the securities and cash are made available for them. The record shows the composition was put into effect (6, 179, 305) as far as it could be prior to 1947, and hence it became binding upon creditors.

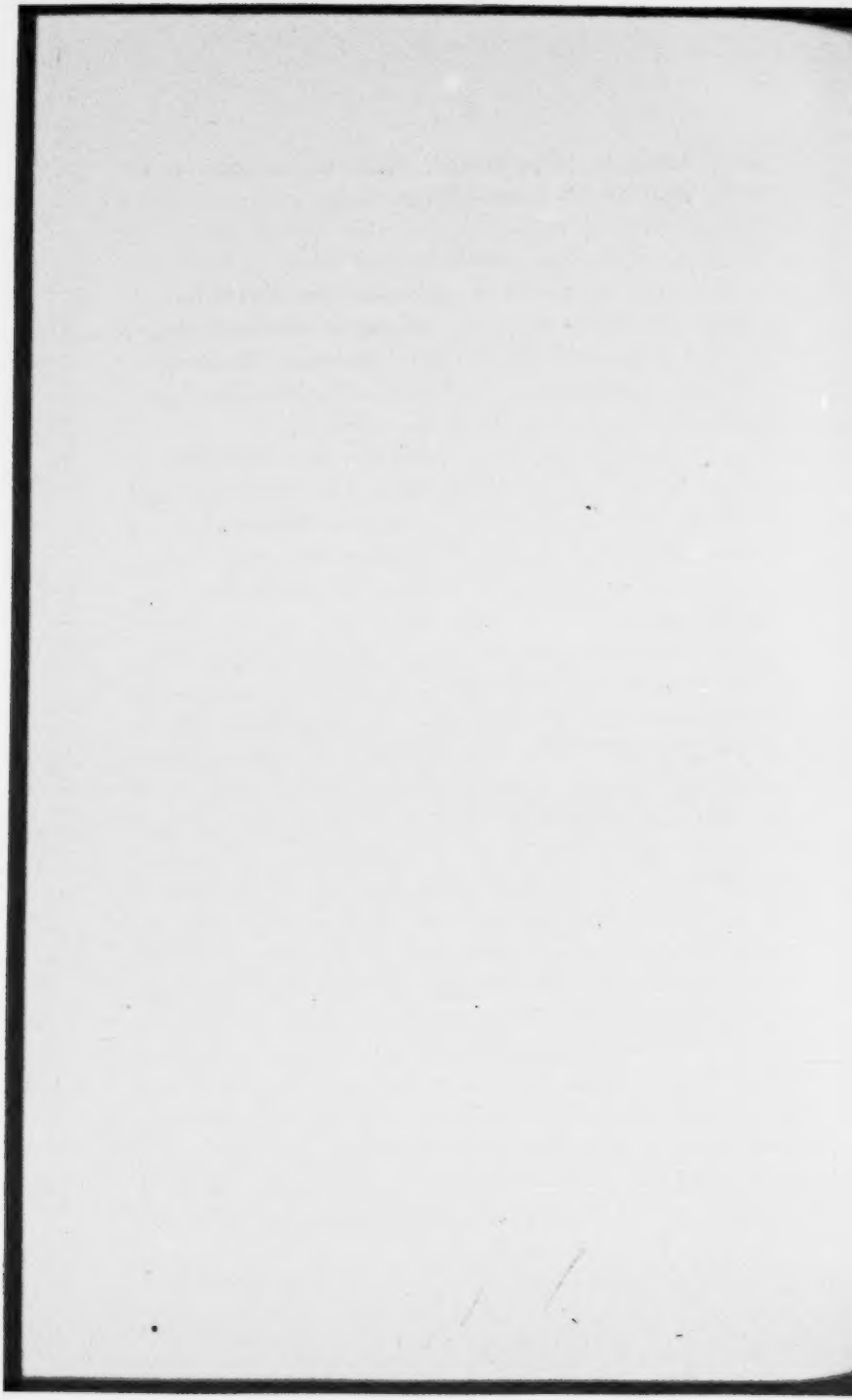
The final decree provided for in Sec. 403 is merely a supplementary decree, determining the fees and costs to be allowed.

The principal apprehension which induces us to file this brief is an innuendo contained in the closing paragraphs

of respondents' brief, to the effect that the decree did not really determine that the additional assessments provided for in paragraph 8 of the plan of composition should be levied on all lands in the district and political units, and that such additional levies were within the law. As shown by the concise statement in the petition and the opinion of the court, tax resources of the district were: (1) unpaid installments upon the original assessments, which were a lien from the organization of the drain district and which were extended through the operation of what was called the supplemental assessment roll of 1937; (2) the power to levy additional assessments, which all parties and the bankruptcy court assumed could be levied on all lands privately owned at the time such levy should be made. As to the former, there necessarily would be a marked shrinkage because liens for the unpaid balances would be cancelled as soon as the state acquired title to lands at tax foreclosure sales, and there would be but a small salvage as a result of their sale by the State Land Office Board (296). The additional assessments to commence in 1947 were designed to augment the former to an amount which would service the refunding bonds. After determining the amount which could be effectively levied each year under the supplemental roll, the additional levy should be added thereto in such a sum that the combined amount would provide for recurring interest, and build a sinking fund for ultimate retirement. Paragraph 8 of the plan of composition did not leave open for future consideration the question of whether this full amount of additional levies could be made. The decree which the lower court affirmed (203) is obviously inconsistent with paragraph 8, and intended so to be, on the ground that the bankruptcy court lacked power to adjudicate questions of state law pertaining to

the taxes which could be levied. This we contend is an erroneous decision of a federal question.

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Respondents

Brief Opposing Petition for Certiorari

I

Opinions of the courts below.[*]

The opinion (303) of the court below is officially reported as Oakland County Drain Commissioner v. City of Royal Oak, 325 Mich. (adv. sheets) 298, and unofficially as Clark,

[*]

Unless otherwise plainly indicated by the context, numbers in parentheses throughout this brief, refer to pages of the printed transcript of the record.

County Drain Commissioner, v. City of Royal Oak, 38 N.W. 2d 413.

The opinion of the trial judge will be found in the transcript of the record (193).

II

Counter-Statement on Jurisdiction.

We may concede that the writ of certiorari was applied for within 90 days after entry of judgment in the court below, pursuant to Title 28, U.S.C., § 2101 (c).

Petitioners invoke the jurisdiction of this Court, Title 28, U.S.C., § 1257, on the ground that in the court below, rights, privileges and immunities were specially set up and claimed by them under an interlocutory decree (42) of the district court of the United States for the eastern district of Michigan, southern division, approving a plan proposed in proceedings for composition by a public debtor, *viz.*, the Royal Oak Drain district, Oakland County, Michigan, all pursuant to Title 11, U.S.C., § § 401-403.

Whether the Court should exercise such jurisdiction in this cause depends largely, we assume, upon the substance or lack of substance in such claim, and whether the decision of the court below is plainly right and in accordance with well-considered judgments of this Court in similar cases, Supreme Court Rule 38 (5).

It is our position:

1. The Supreme Court of Michigan did not decide a federal question of substance.

2. The court below decided the question presented in petitioners' "reasons and grounds of appeal" (206) in a way which is in accord with applicable decisions of this Court, Supreme Court Rule 38 (5 [a]), decisions which, we respectfully submit, control the issue here:

Municipal Investors Ass'n v. City of Birmingham, 316 U.S. 153, affirming 298 Mich. 314, 299 N.W. 90;

Keefe v. Clark, Drain Commissioner, 322 U.S. 393, affirming 306 Mich. 503, 11 N.W. 2d 220.

III

Counter-Statement of the Matter Involved.

We respectfully note, Supreme Court Rule 27, the following inaccuracies and insufficiencies in petitioner's statement:

1. It is said, petition, p. 3, that when the decree of confirmation (42) was entered by the bankruptcy court on the 6th day of February 1941, "no question was * * * entertained as to these lands being fully taxable for all purposes as soon as such restoration (to private ownership) should occur. There were then no court decisions dealing with the subject, * * * and the applicable statutes * * * seemed to justify the conclusion that all privately owned lands, irrespective of their source of title, would be subject to the additional assessments provided in paragraph 8 of the plan of composition".

Counsel overlook the fact that the impairment argument was presented in a decision of the court below on September 6, 1940,

Baker v. State Land Office Board, 294 Mich. 587,

wherein it was held, *inter alia,* that purchasers of municipal bonds are assumed to have purchased with the knowledge that the lien upon the property securing taxes and assessments for the payment thereof might be displaced, Act 155, Pub. Acts 1937, as amended.

That the *Baker* case, *supra,* foreshadowed decision in *Keefe v. Oakland County Drain Commissioner,* 306 Mich. 503, clearly appears from the opinion of this Court affirming the judgment of the Michigan supreme court, 322 U.S. 393, 397, note 3, wherein it is said:

> "The Michigan Supreme Court has described vividly the intimate relation between the power of the State to remove encumbrances from tax-delinquent lands and the welfare of the public. *Baker v. State Land Office Board,* 294 Mich. 587, 592-594".

2. It is thought essential to a clear understanding of the question presented, that we set forth in chronological order a short, concise history of certain judicial decisions in closely-related cases which grew out of legislation enacted for the purpose of solving Michigan's tax problem during the years of depression, as well as in connected cases involving the bond issue now considered:

Jan. 14, 1937:

Royal Oak Drain District v. Keefe, 87 F. 2d 786, was a suit by non-resident bondholders brought in the district court of the United States for the eastern district of Michigan, southern division, against the Royal Oak Drain District and others. Both the district court and the circuit court of appeals, 6th Circuit, upheld the right of the drain district to construct the drain in question, to issue bonds and levy assessments therefor.

We note that in the cause aforesaid, the court reserved jurisdiction for the purpose of carrying its decree into effect, and to grant any further relief necessary.

In the case at bar in the court below, cross-appellants (Cities of Pleasant Ridge and Huntington Woods and others, *not the petitioners*) claimed that the decree entered in the cause aforesaid, 87 F. 2d 786, reserved judgment to adjudicate further rights of the parties, and they contended that the State courts had no jurisdiction as it would be a collateral attack on the decree of the Federal court. The court below held that this was not a collateral attack since entirely new questions were raised in the case at bar. Since the petitioners do not raise it here, that question is not present.

Feb. 6, 1941:[1]

In the Matter of Royal Oak Drain District, pending in the district court of the United States for the eastern district of Michigan, southern division, an *interlocutory decree* was entered (42) in proceedings for composition by a public debtor, namely, the Royal Oak drain district, pursuant to chap. 9 of the bankruptcy act, Title 11, U.S.C., § §401-403, approving a plan of composition, as amended,[2] which had been proposed by the district.

With respect to such proceedings, it may be noted:

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[1]

Meanwhile, on July 3, 1937, Michigan's "scavenger sale" law, so-called, discussed by this Court in a subsequent decision, 322 U.S. 393, became effective, and this statute was amended June 15, 1939, by Act 244, 1939.

[2]

The court suggested (43) these amendments.

(a) although the decree adjudges (44) that "the petitioner is authorized by law to take all action necessary to be taken by it to carry out the said plan of composition, as amended", the record does not clearly indicate that in this regard the action was adversary, or that any objecting creditor raised the question of law later decided by the court below, 298 Mich. 314, 306 Mich. 503, and by this Court, 322 U.S. 393, *i.e.*, whether Michigan's State land office board act ("scavenger sale") of 1937, as amended in 1939, was valid as against such bondholders; therefore, we think, it may be said, that the district court merely assumed that the drain district was authorized to levy additional assessments against parcels of land title to which had passed through the State to private ownership, relieved of such incumbrances; and

(b) the decree was "interlocutory" (42) and the court retained jurisdiction (45) for the purpose of determining fees, expenses, etc., "and for any other purpose or purposes in connection with the completion of the consummation of said plan of composition, as amended, and for any other purpose or purposes contemplated by the Federal Bankruptcy Act", and so far as this record discloses, no final decree was entered.[3]

June 30, 1941:

Municipal Investors Association v. City of Birmingham, 298 Mich. 314, 299 N.W. 90, denied a writ of mandamus to compel the city and others to assess additional taxes on certain lands in said city to pay special assessment bonds issued in connection with a street-paving project, thereby

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[3]

The writer of this brief is not informed whether this is an actual fact, though the record shows that the petitioners rely upon the "interlocutory decree".

upholding the constitutionality of Michigan's State land office board act, as amended,[4] as well as an amendment to the general property tax law of that State.[5] The court held, Syl. 6,

> "In providing for the cancellation of liens for taxes and special assessments on real estate upon vesting of absolute title in the State after sale for delinquent taxes and failure of former owner to redeem and for disposition thereof by the State at the so-called scavenger sale, neither the general property tax law nor the State land office board act contravenes the requirements of the Constitutions of the State or United States forbidding the impairment of the obligations of contract (U.S. Const. art. 1, § 10; Mich. Const. 1908, art. 2, § 9)".

April 27, 1942:

Municipal Investors v. Birmingham, 322 U.S. 153, affirmed the judgment of the court below in 298 Mich. 314, 299 N.W. 90, though it did not pass upon the constitutional question presented. The Court held in substance that various provisions of Michigan statutes, did not establish a contractual right in the bondholders to require that the municipality, in order to meet deficiencies in the collection of assessments, shall re-assess lots in the improvement district which had been sold for non-payment of the original assessments.

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[4]

Act No. 155, Mich. Pub. Acts of 1937, as amended by Act No. 244, Mich. Pub. Acts of 1939.

[5]

Act No. 114, Mich. Pub. Acts of 1937, amending general property tax law.

Oct. 11, 1943:

Keefe v. Oakland County Drain Commissioner, 306 Mich. 503, 11 N.W. 2d 220, modified and affirmed a declaratory judgment which determined that the defendants were not obligated by the Michigan drain law,[6] to levy an additional assessment to cover a deficiency in a drain tax.

The plaintiffs were owners of bonds which were part of the original issue in 1927 of $300,000 to finance the construction of a storm sewer drain.

The Michigan Supreme Court held, *inter alia,* that lands which have passed through "scavenger" sales were exempt from *future* assessments for prior benefits to the land.

May 22, 1944:

Keefe v. Clark, Drain Commissioner, 322 U.S. 393, affirmed the judgment of the court below in the cause aforesaid, 306 Mich. 503, 11 N.W. 2d 220. The Court held that the Michigan statute upon which the owners of special assessment bonds there relied (see footnote 6), and upon which the petitioners in the case at bar *now* rely, petition, pp. 4-5,[7]

> "dealing with the levy of an additional assessment in the event that the bonds are not paid in full at matur-

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[6]

Act No. 316, chap. 10, § 18, Mich. Pub. Acts of 1923, as amended by Act No. 331, 1927 and Act No. 129, 1939. See Mich. Stat. Ann. (Henderson), 1947 Cum. Supp. § 11.104. Now published in Mich. Comp. Laws 1948, Vol. 2, § 270.18.

[7]

The statute cited in the petition, p. 4, is Act No. 129, Mich. Pub. Acts of 1939, which amended § 18 of chap. 10 of the Michigan drain law cited in note 6.

ity, did not secure to the bond owners any right which was impaired by later statutes providing for sale by the State, free of all encumbrances, of land for unpaid taxes; and the later statutes did not impair the obligation of their contracts in violation of the Federal Constitution".

IV

Question Presented.

The question for immediate consideration, of course, is whether the Supreme Court of Michigan decided a federal question of substance, and whether the decisions cited above control the issues involved.

V

Reasons for denying writ.

1. It might be said, without being too captious, there is some doubt whether a federal question, as such, was actually raised in the trial court or in the court below, whether any title, rights, privilege, or immunity was "especially set up or claimed" under a statute of the United States.

(a) Appellants' "reasons and grounds of appeal" set up in the court below (206) do not indicate that a Federal question is there presented; no mention is made of the interlocutory decree of the United States district court in the bankruptcy proceedings; the bankruptcy act is not cited; and the only reference is to certain paragraphs of the drain commissioner's order of April 17, 1941.

(b) Nor did petitioners' answer (69-77), filed as defendants in the circuit court, indicate such a claim; it was "their desire to have the programme laid out in the drain commissioner's order of April 17, 1941 fully performed, irrespective of whether there may be ultimate shortage or not" (70).

They insisted in their answer (71) that when a drain district "does issue refunding bonds and certificates of indebtedness, and compels their acceptance by creditors by virtue of proceedings taken by it in bankruptcy proceedings, it thereby accepts the provisions made applicable to such securities by Act 129 of Michigan Public Acts 1939",

> "and all lawful orders made by the drain commissioner under it, and same become binding upon all property owners in the district and upon all political subdivisions subject to at large assessments for the drain. Defendants allege that additional assessments may be levied against all lands in said district which are otherwise taxable, and to the extent that any lands become exempt by any stutute or proceedings under it, the loss of resources for debt payment must be absorbed by the *remaining* lands and the political subdivisions subject to at large taxes". [Emphasis, ours].

This, we respectfully submit, is not an unqualified reliance upon Federal rights; it is based upon a Michigan statute, the same law which this Court later held, 322 U.S. 393, did not secure to bond holders any vested rights.[8]

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[8] It is true that appellants, in their brief, contended that the decree of the bankruptcy court was binding upon the drain commissioner.

2. The court below expressed two opinions, 325 Mich. 311, 38 N.W. 2d 417-418, on the subject: (a) they doubted "if the taxpayers were bound by the decree of the Federal court in the composition proceedings", and (b) they held that even though taxpayers were so bound, "such decree wound not be binding as to the rights and duties of the drain commissioner *under State laws*" (emphasis supplied), the construction and interpretation of which "are binding on the Federal courts".

We respectfully submit the Michigan Supreme Court were right on both counts of their decision:

(a)

The decree of the bankruptcy court was not binding on taxpayers or State taxing officers.

The controversy, if any, was between the petitioning drain district, which sought approval of the proposed composition plan, and objecting creditors. Taxpayers, the purchasers of land offered by the State at "scavenger" sale, prospective purchasers of such land, State taxing officers, and members of the State land office board, were not parties to the composition proceedings, nor were they represented by counsel.[9]

That the State itself was virtually interested in the subject-matter of subsequent levies upon property title to which had or would vest in purchasers at the "scavenger" sales, appears from the opinion of the court below in the

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[9]

While it is true that the public debt commission approved the refunding bonds, there was nothing in the act of their creation, Act No. 13, Mich. Pub. Acts 1932, Ex. Sess., which militated against the doctrine of Keefe v. Drain Commissioner, 306 Mich. 503.

Keefe case, which was summarized by this Court, 322 U.S. 393, 396, as follows:[10]

> "Emphasizing the serious consequences of such a hobbling of the State's powers to meet pressing problems, the Court pointed out that the powers of the State to sell tax-delinquent lands free of the burden of assessments for completed drain projects was essential not only to protect the bondholders themselves but to protect the public interest. Without power in the State to offer an attractive title to prospective purchasers, the Court found, many of such lands would remain tax-delinquent and thereby be rendered valueless for all public revenue purposes, including drain assessments. The Court declined to read into the statute relied upon by appellants any purpose to permit drain districts to surrender the State's sovereign power to provide for the sale of tax-delinquent property free of encumbrances. It held that under the Michigan law in effect when appellants' special assessment drain bonds were issued the bondholders' 'maximum security' for payment of assessments against drain district lands was the parcels of land themselves, and that when the bondholders received their fair share of the proceeds derived from the tax sale of any particular parcel they had received everything to which their bond contracts entitled them. *Keefe v. Oakland County Drain Comm'r,* 306 Mich. 503, 511-512, 11 N.W. 2d 220."

We fail to see how the decree of the court could possibly bind the taxpayers of the taxing unit, or determine the

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[10] This was in answer to the argument that the Michigan legislature was powerless to provide that purchasers of tax-delinquent property in the drain district be exempt from a deficiency drain assessment.

rights of those persons who later acquired title from the State at "scavenger" sales.

(b)

Nor was the decree binding as to the rights and duties of the drain commissioner under State laws.

If the decree of the district court be construed [as petitioners insist] to constitute a final adjudication respecting the duties of the drain commissioner under Michigan statutes as interpreted by the Supreme Court of that State in an opinion affirmed by this Court, it would now require him to violate such laws, a wholly inconveivable situation.

Be that as it may, however, it manifestly appears that the district court did not adjudicate the *precise* question presented in the pending petition for certiorari. The bankruptcy court did find (44), as indeed it was required by law, Title 11, U.S.C. § 403, to do, that the petitioner was "authorized by law to take all action necessary to be taken by it to carry out the * * * plan of composition, as amended". Which meant, of course, that the drain district was so authorized by *State law, United States v. Bekins,* 304 U.S. 27. And it is also obvious that the State of Michigan had given its consent to the filing of a petition under the bankruptcy law, Act No. 72, Mich. Pub. Acts of 1939. That act provided, in part:

> "The governing authority of any such taxing agency having authority to levy taxes to meet the obligations to be affected by the plan of composition may file the petition and agree upon any plan of composition authorized by said act of Congress, and may include in such plan of composition any terms and conditions relating to readjustment, alteration, extension and reassess-

ment of taxes and assessments which they may deem advisable. Such plan of composition, when approved by the court as provided in said act of Congress, shall be binding upon such taxing agency or instrumentality".

It should, we think, be born in mind that the same legislature which enacted Act No. 72, *supra,* effective May 3, 1939, also amended the State land office board ("scavender sale law") by passing Act 244, Mich. Pub. Acts 1939, effective June 15, 1939, and, we respectfully submit, all of these statutes should be construed as constituting one harmonious system of tax enforcement.

Although it may have been believed by all parties concerned that the Michigan tax statutes cancelled only special drain assessments against state acquired lands, which had already been made (including future due installments thereof), but did not cancel the right to make future drain assessments against lands restored to private ownership, this theory is not clearly expressed in Act No. 72, *supra,* nor in the plan of composition (38), nor in the decree (42) approving it. Paragraph 8 of the plan (38-39) provided that the spread of special assessments should be "(exclusive of any part thereof cancelled by the terms of Act No. 155 of the Public Acts of 1937, as amended)", and that deficiency assessments each year "shall be levied under the provisions of Act No. 129 of the Public Acts of 1939 against the various political subdivisions and parcels of land in the special assessment district, in proportions as originally assessed".

This language, we respectfully submit, left the Supreme Court of Michigan free to construe, interpret and apply the provisions of the "scavenger" sale act, as well as the terms of Act No. 129, Mich. Pub. Acts 1939, and to hold, as they later did in the case of *Keefe, supra,* that lands which have

passed through "scavenger" sales were exempt from future assessments for prior benefits to the land.

Otherwise, the power of the State to meet pressing problems of the nature referred to in the *Keefe* case, 322 U.S. at 396, would be hobbled by a strained construction of the decree of the bankruptcy court.

Our position, therefore, is that the district court did not decree, and the plan of composition which it approved, did not provide that lands which had passed through "scavenger" sales would be subject to the reassessment mentioned in the plan. Nor was the question presented for decision on clearly-defined issues in the composition proceedings.

VI

Conclusion.

We, therefore, respectfully submit that the petition for writ of certiorari should be denied.

Respectfully Submitted,

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